Postal Regulatory Commission
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CONSUMER
POSTAL
COUNCIL

Ref.: Order No. 4257, Docket No. RM2017-3

March 1, 2018

Dear Postal Regulatory Commission:

These comments pertain to the December 1, 2017 order [Order No. 4257, Docket No. RM2017-3] on the statutory review of the system for regulating rates and classes for market dominant products. The Postal Regulatory Commission (PRC) concluded that the rate system has not achieved necessary objectives and issued proposed rulemaking to address shortcomings.

Our overall assessment is that these findings are at best pre-mature and very likely to be proven incorrect in coming years. With the proposed order, there is a high likelihood that postal costs will increase significantly for consumers; Postal Service losses will mount; and operating efficiencies and modernization will fail to take place. This will place major stakeholders in a worse position than today.

Specifically, we respectfully submit these seven contentions.

The Postal Service should develop a comprehensive, flexible and credible business turnaround plan that will address its core operating challenges and the vision it has for implementing positive change over the next three to five years.

The turnaround plan should address major issues, including the strategies to realize the following.

- Optimal ways to reduce current and future retirement expenses and, even more importantly, to improve the investment performance of retirement plans
- Operating cost reductions and improved efficiencies
- Capital expenditures: where these should be made and how they should be prioritized
- Technology which can further improve the efficiency and profitability of monopoly services

Without such a plan, the PRC effectively will be issuing its order in a vacuum.

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The Postal Service has a long and well-documented record of failing to implement sufficient cost reductions and efficiencies. These practices must be changed before asking for more postal consumer funds.

The PRC's own words from the December 1 order are clear and powerful in this regard, "The Commission has repeatedly advised the Postal Service that it must 'do a better job of quantifying the savings from its cost reduction initiatives.' In the joint Periodicals Mail Study, the Commission noted the Postal Service's 'inability to capture efficiencies in flat mail processing' and stated that '[s]ubstanial opportunities for increasing the efficiency of flat mail processing and transportation exist.' The Commission further stated that "[o]ver the past decades the Postal Service has introduced many programs designed to capture some of these efficiencies,' but that it was 'unclear how successful these programs have been.'" (page 206 of the PDF of the order).

Regarding the creation of a Postal Service program to better align retail customer service, the PRC said, "The Commission found that the initiative was not likely to optimize the retail network and there was no effective mechanism to accurately identify cost savings" (page 204).

Concerning an efficiency initiative to level the volume of mail throughout the week the PRC was again critical. It said, "The Commission found that the plan needed further development and recommended, among other things, that the Postal Service perform a cost-benefit analysis at the national level and develop a plan for measuring cost reductions" (page 205).

There is a clear, disturbing and ongoing pattern of the Postal Service failing to meet cost cutting and efficiency goals. And, there does not appear to be any consequence for failing to do so. There must be a fundamental change in the Postal Service's culture on costs and operating efficiency, and related business changes, before postal consumers are asked to pay significantly more.

There are important questions as to whether the Postal Service is properly accounting for institutional costs on its product lines.

The allocation for competitive products' contribution to institutional costs is set by the PRC at 5.5 percent and has not changed since 2007. Yet competitive products have consistently grown and now account for nearly 30 percent of the Postal Service's business. In quarterly financial press releases and other outlets, Postal Service management consistently touts the future opportunities from packages and competitive products.

Yet, the figure for the institutional cost contribution requirement for competitive products will not change until at least Fiscal Year 2020. Per the February 8 order [Order No. 4402, Docket RM2017-1], the PRC said, “under the proposal, the Commission would calculate and report the appropriate share for FY 2020 as part of the FY 2018 ACD” (page 102 of PDF).

Given the importance of this figure, and the potential that it could significantly change, the December 1 recommendations should not be implemented until this key financial input is determined.

In addition, the Postal Service should be encouraged or directed to consider forming a stand-alone packages unit so that costs are better monitored and managed.

The Postal Service should be directed to concentrate its focus on monopoly products which enable it to meet its universal service obligation and which are today at the core of its mission to the public.

As the Postal Service says in its Fiscal Year 2018 Form 10-K report, “Market-Dominant products account for approximately 70% of our annual operating revenues.” This is approximately $48.7 billion annually.

The Postal Service also says in this report that first-class mail is “our most profitable service category”.

Another market dominant product, marketing mail, has a bright future as discussed in the 10-K, “Marketing mail has generally proven to be a relatively resilient marketing channel, and its value to U.S. businesses remains strong due to better data and technology integration.”

These operating practices and strengths of the Postal Service should be better understood and encouraged. Instituting large price increases in these areas could meet with high-levels of consumer and business customers’ opposition and thereby threaten the positive fundamentals in these areas.

There needs to be a study of the impact of the price increases. Since this has not taken place, implementing large price increases could be catastrophic and make the current financial challenges much worse.

It is disconcerting that there have been no studies concerning the impact of the proposed price hikes on the Postal Service’s business. In the digital age, postal customers certainly have other options and a large price increase could be the tipping point for reducing business with the Postal Service. This seems likely given the financial concerns of those Americans on reduced and fixed incomes and very tight profit margins that many direct mailers have.

The Postal Service's retirement plans need to be restructured so that they receive significantly higher average annualized returns, comparable to pensions for state government employees.

On September 20, 2017, the Postal Service's Office of the Inspector General (OIG) issued a very important report, Postal Service Retiree Funds Investment Strategies. Under federal law, the Postal Service can only invest its retirement funds in special-issue Treasury bonds, that have had returns of 3-4% in recent years.

These returns have significantly and perennially underperformed the returns that state pension plans for government employees have achieved. OIG warned that if the Postal Service continues with its current approach its retirement plans will continue to underperform in the future.

Just as businesses know that a poorly performing pension plan will have a major impact on earnings and other business performance, this is also the case with the Postal Service. It is imperative that a turnaround plan for the Postal Service champions new legislation which will allow retirement plans to be invested in equity markets.

Since Fiscal Year 2012, the Postal Service has defaulted on $33.9 billion of retiree health benefits and has a cumulative funding deficit of $73.4 billion in its three retirement plans.

These deficits would not exist had the Postal Service invested for the past decade as state pension plans do, as the following illustration helps demonstrate.

For the 12 months ending September 30, 2017, the New York State Common Retirement Fund returned 12.4 percent compared with a maximum of 4 percent for the Postal Service's retirement accounts. The New York State return is typical of a diversified pension fund return during this period.

Had the Postal Service invested its $338 billion in retirement assets the way New York State did, it would have accumulated an additional $28.7 billion in the 12-month period alone, reducing its shortfall by 39%.

OIG points out that going forward the challenges will be greater for the Postal Service as retirement costs are rising and funding shortfalls are significant. There is urgency to provide the Postal Service with the same, typical investment options that state government pensions have.

Before allowing for any Postal Service cost increases above the rate of inflation, a full audit and assessment needs to be done to end subsidized international mail, especially e-commerce that is flooding the U.S. from China.

Due to U.S. participation in the international mail agreement structured by the Universal Postal Union (UPU), it costs less to send a package from China to the United States than to send a package within the U.S.

The PRC found that for Fiscal Year 2016, the terminal dues program cost the Postal Service $134 million. Losses are expected to be higher for Fiscal Year 2017.

Before American consumers are asked to pay significantly higher prices, the Postal Service should revise its Negotiated Service Agreement with China to end such subsidizes. In addition, the U.S., through the actions of the State Department and the PRC, should inform the UPU that the agreement should immediately be re-negotiated or that it is terminating its participation.

Since 2003, the mission of the Consumer Postal Council has been to champion world-class postal services by promoting programs and policies that increase productivity, transparency and eliminate distortions and inefficiencies caused by monopolies.

We appreciate the opportunity to provide these comments and thank the Commission for its diligent and ongoing work.

Sincerely,

DocuSigned by:
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